



Snapchats for Boards

by TPA Global

BEPS for Boards



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1. What is BEPS and how does it affect multinationals?

The Project on Base Erosion and Profit Shifting (BEPS) – encompassing 15-action BEPS plan aimed to curb tax avoidance – was initiated by the Organization for Economic Co-operation and Development (OECD) and supported by G20 world leaders in 2013. Its final outputs on October 5, 2015 resulted in 15 reports addressing areas, perceived to have the greatest potential for abuse by multinational, which among others will have a substantial impact on transfer pricing (TP) going forward¹. This new initiative by OECD marks the biggest change international tax regulation has been undergoing in a recent generation.

The general goal of the BEPS Project is to drive tax transparency to all stakeholders by enhancing global sharing (e.g., mandatory filing of country-by-country reporting) and ensuring that multinational enterprises are taxed 'where economic activities take place and value is created'.

Multinational firms, already facing a multitude of challenges, seem to be hit hard by OECD's new initiative. OECD's BEPS Project, especially through its two items covering intangibles and documentation, creates an additional compliance burden. Given the scale of change foreseen, Tax & TP compliance costs for multinationals, if expressed in quantitative terms, are expected to increase by up to 50%.

In the light of BEPS adding to the pressure on multinationals, it is critical for board members to start thinking through the much more efficient ways for tackling new regulatory challenges to stay in control over Tax & TP risks post BEPS. Looking forward, full standardization and automation of Tax & TP processes must become an increasing area of focus on the boardroom agendas.

2. What are the practical implications of BEPS to your firm?

The elimination of double taxation is very low on the governments' and tax authorities' agendas. In fact, OECD has no priority to tackle double taxation in the next 10 years. Generally, the approaches chosen by OECD are believed to cause increased complexity as they involve high subjectivity and discretion in their application by tax authorities. As a result of this, there is a high probability that multinationals will witness an increase of their Effective Tax Rates (ETRs) by 10-20% above 'nominal tax rates'.

Considering the above, leading multinationals are now taking a much more proactive and forward-looking approach to their tax policies and dispute avoidance & resolutions. They do that by starting to identify the activities that may become unacceptable post BEPS. A regular review of tax policies with the board members is recommended in order to:

¹ Please note that some of the proposed BEPS measures are not yet finalized and will be further addressed in the OECD reports planned to be issued in the subsequent years.

- Gain a better understanding of the various existing intercompany financial and non-financial structures which post BEPS need to be eliminated or transitioned to new ones;
- Assess the mismatch between ETR shown on the income statement and average expected tax rate based on where sales are made to see if it does not cause any reputational damages;
- Appropriately plan the management of tax & TP processes in order to avoid compliance costs doubling in the long-run; and
- Drive meaningful facts-based communication and disclosure of tax & TP practices among both internal and external stakeholders.

The immediate lessons that all multinationals should take away from the BEPS Project is that:

- Based on BEPS there is no time to delay your actions;
- Tax and TP is an integral part of corporate strategy; and
- Boardrooms must take a conscious stance on tax & TP matters by encouraging structured and frequent reviews of BEPS sensitive topics.

3. Boardrooms agenda on BEPS

The list of ten questions provides structure to an engaged dialogue between board members and tax/ TP executives. For a one page summary of BEPS key focus areas, please refer to Appendix 1.

The list of questions on 'Tax agenda' post BEPS:

1. As a result of BEPS will there be a risk that the firms' name will be on the front page of any newspaper on tax matters? If so, please quantify the probability and what in-house tax is doing to mitigate such risk.
2. Are compensations to all group companies aligned with their 'value creation' to the firm's value chain as BEPS seems to indicate?
3. Are we afraid of sharing tax positions with all relevant stakeholders without reservations under BEPS? For example: the country-by-country reporting does report all data points on a firm's value chain to all tax inspectors involved.
4. How do we control the doubled compliance costs triggered by effort and time spent on BEPS?
5. What is the cost of running the tax function (in-house as well as external advisors) and how do we compare to our peers post BEPS in the planning for the next 2 years?
6. Do we still run hybrid structures, extreme debt positions, tax schemes and tax driven set ups today, which BEPS tries to ban out in the next 24 months? In other words, is there any corporate tax position below an effective tax rate of 15%?
7. Did the in-house tax group do a reset on the organizational and operational set up to be BEPS ready? If so, please list the Top 3 major initiatives undertaken or achieved.
8. How do we keep tax authorities at a distance, while not turning the in-house tax function in one big tax/ transfer pricing compliance exercise under BEPS?

9. How much time (% of total) does the-house tax team spend on communication with internal and external stakeholders on BEPS risk management measures?
10. Which Top 10 countries are most vulnerable from a tax/transfer pricing perspective and how do we handle priorities in these countries?

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Appendix 1: Summary of BEPS key focus areas

BEPS focus area	Explanation
Country-by-country reporting and TP documentation	Detailed templates and indexes of TP documentation that needs to be filed in each country have been agreed. This also includes a Country-by-Country reporting which requires MNEs to annually disclose information relating to the global allocation of income and taxes paid.
Transfer pricing	Additional recommendations are created by OECD to disallow attribution of significant profits to group entities within a multinational claiming to perform activities (e.g., management of intellectual property), unless it is proved to have the people and capacity to do so.
Hybrid instruments and entities	Additional recommendations are created to overcome tax avoidance triggered by country by country treatment differences in classification of the entities (e.g. considered to be a company in one country but a partnership in the other), or instruments (e.g. treated as debt or equity)
Denial of interest deductions	Additional recommendations are created for countries to establish a fixed cap for deduction of interest, within a range of 10%-30% of either EBIT or EBITDA.
Tax incentives or preferences	A strengthened requirement is suggested to show substantial economic activity in the country, and a nexus between expenditure on that activity and the income benefiting from the preferential tax regimes (e.g., patent/ innovation boxes).
Taxable presence	Revisions are proposed to the definition of the taxable presence (i.e., tax treaty definition of a permanent establishment) which will make it more difficult for a firm to avoid attributing profits from sales in a country if it has an affiliate or agent there that concludes the contracts.
Mandatory disclosure schemes	Countries are encouraged to introduce requirements for disclosure of aggressive or abusive transactions, arrangements or structures, either by their promoters or users or both, with recommendations for rules targeting international schemes.